



**Revenue Laws Study Committee
February 12, 2020
Room 1228 Legislative Building
9:30 AM**

The Revenue Laws Study Committee met on Wednesday, February 12th at 9:30am. The meeting was held in Room 1228 of the Legislative Building in Raleigh. Senator Paul Newton presided. Members present were: Senator Paul Newton, Chair, Representative Julia Howard, Chair, Senator Ralph Hise, Vice Chair, Representative Stephen Ross, Vice Chair, Senator Jerry Tillman, Vice Chair, Representative Kelly Alexander, Senator Harry Brown, Representative Dana Bumgardner, Senator Ben Clark, Senator Chuck Edwards, Senator Toby Fitch, Senator Kathy Harrington, Representative Chris Humphrey, Representative Stephen Ross, and Representative Harry Warren. Cindy Averette, Trina Griffin, and Greg Roney of the Legislative Analysis Division and Rodney Bizzel, Denise Canada, and Johnathan Tart of the Fiscal Research Division were also present. Justus Cochran, Cameron Dawson, and Cody Huneycutt, Committee Clerks, were present.

I. Welcome and Approval of Minutes from the January 29, 2020 Meeting

Senator Newton called the meeting to order at 9:30am and welcomed members, staff, and visitors in attendance. Senator Newton introduced the Sergeants-At-Arms, Marvin Lee, David Leighton, Glen Wall, Linda Matthews, and Billy Fritscher. Senator Newton summarized the agenda and clarified that the sales tax issues were just for discussion and that the committee would not be voting on a specific formula.

II. Committee Recommendation on Draft Proposal: IRC Update

Senator Newton recognized Cindy Averette, Legislative Analysis Division to explain a draft proposal on Internal Revenue Code updates.

Following the explanation, Senator Newton opened the floor to questions from the committee.

Senator Newton asked for a motion to approve the IRC Update. Representative Kelly Alexander motioned and Senator Jerry Tillman seconded. The motion carried. A copy of the approved draft is attached.

Senator Newton then asked for a motion to approve last week's minutes. Senator Harry Brown motioned and Senator Ben Clark seconded. The motion carried. A copy of the approved minutes is attached.

III. Digital Property Tax & Online Learning

Senator Newton recognized Trina Griffin, Legislative Analysis Division, to present on digital property taxes on a variety of online learning programs/classes.

Following the presentation, Senator Newton opened the floor to questions from the committee.

Senator Tillman was recognized for a series of questions. First, he questioned the value of the Streamlined Sales Tax Project since there is no limit on what changes can be made. Mrs. Griffin responded that similarities in sales tax collection across states contributed to the Wayfair decision, which

allowed sales tax collection on remote sales. Senator Tillman then made a comment on the perceived effects that cutting taxes has on overall revenue.

Senator Hise questioned what exactly was being taxed. He made references to tuition and online memberships and asked whether the state would be taxing a membership or a specific class. Mrs. Griffin responded that tuition is not taxed and digital property included in that tuition would also not be taxed. She made distinctions between different types of online courses, classes, and programs that the committee could decide to tax.

Senator Brown questioned whether there must be a charge on the class for a tax to exist. Mrs. Griffin answered that it would depend on the specific scenario. She explained that an organization may have had to pay taxes on the initial purchase before offering the class. However, she clarified that a charge would have to exist at some stage in order for the digital property to be taxed.

Senator Hise provided an example of realtors providing courses to members of their association and questioned whether providing a digital service would make the membership fee taxable. Mrs. Griffin clarified that memberships are not taxed and offering free digital property would not make it taxable. She provided the company Peloton as an example of a membership bundle where some items may be taxable and some are not. She explained that when the majority of that bundle is taxable, then everything is taxable.

Representative Warren commented on how broadening the sales tax base could allow for cutting other taxes. He questioned whether there was a revenue estimate for digital property taxes. Mrs. Griffin responded that fiscal staff did not have an estimate yet. She pointed out that the change was made effective October 1st, 2019 and that some organizations were not yet collecting and remitting sales tax.

Senator Newton commented that, in his opinion, the State should not be taxing individuals in pursuit of a new degree or certificate. However, with respect to expanding the sales tax base, he mentioned that a line could be drawn on what digital property to tax.

IV. Local Option Sales Tax (LOST) Issues

a. Modernizing the State's Local Sales Tax Division

Senator Newton recognized Denise Canada, Fiscal Research Division, and Ernest Irving, Department of Revenue, to present on distribution of local sales tax and possible steps for modernizing the distribution formula.

Following the presentation, Senator Newton opened the floor to questions from the committee.

Representative Warren thanked Mrs. Canada and Mr. Irving for the presentation, asked whether the county that saw the largest decrease in the new formula was a Tier 3 county, and asked for clarification on the quarter-cent in sales tax mentioned on slide 21. Mr. Irving answered that it was an approximation of how much money the state would be providing. Senator Newton mentioned that the next presentation will include options for an additional local sales tax.

Senator Hise raised concerns regarding the use of ad valorem rates due to the large amount of variability from counties not conducting regular reevaluations. He asked whether there were options for smoothing the rates between reevaluations. Mr. Irving responded that there are mathematical options. Senator Hise followed-up by asking whether including ad valorem would be an incentive to raise property taxes to gain more sales tax. Mr. Irving responded that there would be a correlation between the two.

Representative Bumgardner asked whether the goal was to keep the formula as close to status quo as possible. Mr. Irving responded that the goal would be to move to a formula based on recent data without causing large negative impacts to any individual counties. Representative Bumgardner followed-up by questioning whether it was necessary to go through changes in order to maintain status quo. Senator Newton responded by saying the policy goals of the current formula are unclear and based on old data. He clarified that this discussion was to decide whether steps should be taken to modernize the formula. Representative Warren referred back to his previous question asking which county saw the largest decrease in the new formulas. Mr. Irving answered that it was Burke County. Senator Newton mentioned that the figures would be provided to the committee.

Senator Brown mentioned that, in his experience, the formulas were outdated and that there has been a large disparity in the growth of sales tax revenue between rural and urban counties. He explained that a relatively small amount of money can make a large difference in rural areas.

Cindy Averette, Legislative Analysis Division, referenced Representative Bumgardner's last question on the value of modernizing the formula. She agreed that using the current formula as a baseline would keep distributions relatively the same. However, she explained that moving forward the formula would change dynamically by basing the formulas on current data.

b. LOST Flexibility

Senator Newton recognized Trina Griffin, Legislative Analysis Division, to present on flexibility for local option sales taxes.

Following the presentation, Senator Newton opened the floor to questions from the committee.

Senator Brown commented on the challenge of balancing local options sales taxes with uniformity across the State.

Senator Hise asked if it was possible to, not only allow specific ballot language, but also require maintenance of spending at the current level. Mrs. Griffin answered that it was something that could be tried.

Senator Newton mentioned that he had asked Mr. Irving to return at the next meeting so that members could ask him questions.

V. Draft Proposal: Technical, Clarifying, and Administrative Changes, Part I

Senator Newton recognized Cindy Averette, Legislative Analysis Division to introduce a draft proposal of technical, clarifying, and administrative changes for the members to review.

VI. Adjournment

There being no further business, the meeting adjourned at 11:37 AM. The next meeting will be held on Wednesday March 11, 2020 at 9:30 AM in Room 1228 of the Legislative Building.

Senator Paul Newton
Presiding

Justus Cochran
Committee Clerk